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July 15, 2019

*By electronic submission to regs.comments@federalreserve.gov*

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue N.W.
Washington, D.C. 20551

Attention: Ann E. Misback, Secretary

Re: Control and Divestiture Proceedings (Docket No. R-1662; RIN 7100-AF 49)

Ladies and Gentlemen:

Mitsubishi UFJ Financial Group, Inc. welcomes the opportunity to comment on the notice of proposed rulemaking (the "Proposal")[1] by the Board of Governors of the Federal Reserve System ("Board") that would revise the Board's implementation of the "controlling influence" prong of the Bank Holding Company Act of 1956 ("BHC Act") definition of "control" in Regulation Y and Regulation LL. As stated in the Proposal, the concept of control has two principal purposes under the BHC Act—"…to ensure that companies that acquire control of banks have the financial strength and managerial ability to exercise control in a safe and sound manner" and "…to separate banking from commerce…."[2]

MUFG has participated in and broadly supports the comments in the letters submitted by the Bank Policy Institute ("BPI"), the Institute of International Bankers, the Japanese Bankers Association, and the Structured Finance Association. We wanted to take this opportunity, however, to share aspects of our own experience with the Board's controlling influence framework and the particular implications that framework and the Proposal have for a large Japanese banking organization that is a bank holding company ("BHC") under the BHC Act and a foreign banking organization under the Board's Regulations K and Y ("FBO").

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1 84 Fed. Reg. 21634 (May 14, 2019).

2 Proposal at 21635.

The Board has long administered the controlling influence framework largely on a facts-and-circumstances basis. Although this has at times complicated banking organizations' (and others') compliance efforts, it has also enabled the Board to exercise discretion and tailor its findings to particular cases. Moving to the more detailed presumption-based approach reflected in the Proposal brings clear advantages to the industry in the form of additional certainty and transparency, which we appreciate. At the same time, such automatic presumptions of control at pre-defined thresholds almost certainly will result in control presumptions in circumstances where no controlling influence actually exists. No two investor-investee relationships are exactly the same, and any one-size-fits-all approach will be over- (or under-) inclusive. Such an approach also poses the risk that it will unduly limit the Board's ability to accommodate relationships between non-U.S. investors and their non-U.S. investees that have little or even no connection to the United States, contrary to the express dictates of the BHC Act and the Board's longstanding commitment to the principles of international comity.

The Proposal is a laudable step towards establishing a transparent and workable framework, but, in our view, the Proposal errs on the side of over-inclusiveness. This arises from certain elements of the Proposal that are new, as well as from others that generally reflect a continuation of the Board's existing practice. Striking the right balance in a standardized approach to controlling influence determinations is critical because there are real and detrimental consequences to an over-inclusive approach. There is a significant impact on a FBO (first company) and the investee (second company) if the investee becomes subject to the BHC Act. The FBO becomes responsible from a U.S. regulatory perspective for the investee regardless of the FBO's degree of actual control, and the investee becomes subject to a new regulatory and supervisory framework that may constrain the investee's capacity to compete effectively. As a result, a FBO may decide not to act as a source of capital, which limits opportunities for potential investees. Similarly, an investee may not accept investments from FBOs, limiting the ability of a FBO to make strategic investments in companies, including those that are developing innovative products and services that could enhance the FBO's competitiveness and benefit consumers.

These consequences are exacerbated when the BHC Act framework is applied to investments between non-U.S. companies when the investee has no meaningful U.S. activities. In the context of an FBO investor, the BHC Act is designed to accommodate differences in economic and financial frameworks between non-U.S. and U.S. jurisdictions while also ensuring that the FBO's U.S. nonbanking activities remain consistent with the separation of banking and commerce as that separation has been defined under U.S. law. A given jurisdiction may have made its own determination about the proper division between banking and commerce and established a "control" or similar framework to ensure that division is respected, as is the case in Japan. This determination is based on the specific policy decisions made by the legislature, taking into account the jurisdiction's own specific economic and financial structure and

objectives. Because of differences in legal systems, policies, and practices among countries, specific metrics, such as voting shares, equity ownership, number of board seats, and business relationships, may result in control in some countries, but not others. The Board reviews the legal and regulatory framework to which a FBO is subject in its home jurisdiction when the FBO proposes to establish a U.S. banking presence and has the opportunity to determine, as part of its "comprehensive consolidated supervision" evaluation, whether the framework is consistent with the Board's standards. We acknowledge the need to maintain competitive equity between U.S. BHCs and FBOs, but, in doing so, the Board should take account of the differences between U.S. and non-U.S. legal and economic systems and markets when it applies its control presumptions overseas. This is consistent with general principles of international comity and is expressly recognized in Sections 2(h)(2) and 4(c)(9) of the BHC Act. Indeed, the Board has specifically addressed jurisdictional differences in approach to the separation of banking and commerce in acting on applications under the BHC Act by certain Japanese FBOs, as discussed further below.[3]

In the remainder of this letter, we identify specific areas where, in our view, the Proposal is over-inclusive or challenging to implement and we will recommend changes to mitigate or address the resultant concerns. In addition, we provide recommendations to narrow the scope of relationships caught within the "controlling influence" presumptions in the Proposal without undermining the Board's ability to fulfill its statutory mandates.

Existing Non-Control Determinations

Because of the complexity of, and traditionally fact-specific approach to, control determinations, many BHCs and FBOs historically have sought, received, and relied upon formal and informal "non-control" rulings from the Board or its staff. We assume that any final rule is not meant to call into question such pre-existing arrangements. Of course, a BHC or FBO would need to seek a new non-control determination from the Board or staff (or confirmation that a determination is not necessary) if it were to increase any of the control indicators beyond those covered by the rule if, after such increase, the relationship would trigger a presumption of control.

Treatment of Immediate Family Members

Although the Proposal in many respects is a reflection of the Board's existing interpretations, the definition of "director representative" appears to represent a departure from the Board's historic practice in a way that would present significant

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[3] *See* Board Orders regarding The Dai-Ichi Kangyo Bank, Ltd., The Mitsubishi Bank, Ltd., and the Sanwa Bank, Ltd., Federal Reserve Bulletin (January 1972) at 49-53 ("Japanese Bank Orders").

implementation difficulties without meaningfully advancing the Board's objectives. The element of the definition that would pose the most practical difficulties is the expansion of the definition of "director representative" to include "the immediate family member of any employee, director, or agent of the first company." Taken literally, this means that a BHC or FBO would need to confirm whether each director of any company in which the BHC or FBO holds a voting interest of less than 25 percent is an immediate family member of any single one of its employees, directors, or agents. This would even apply to directors serving before the BHC or FBO made its investment. For a FBO such as MUFG, developing procedures to identify immediate family members of such an immense range of people (MUFG has approximately 180,000 employees) would be an extraordinary undertaking. MUFG expects that in almost all cases, even if an immediate family member of an employee, director, or agent of the first company were identified among the directors of a second company, the family member's presence on the board would be entirely unrelated to any investment by MUFG in the second company. Moreover, MUFG believes that such a family member's presence would not in any way represent an attempt by MUFG to exert a controlling influence on the second company.

We recommend eliminating the immediate family member prong from the definition of director representative. The Board's authority to find control based on other facts and circumstances should be sufficient to address the potential risk that a first company could expand its influence through an immediate family member of an employee, director or agent.

Business Relationships

Including business relationships as a metric in control presumptions is challenging because the same metric applies at a point in time to a wide range of relationships between companies of different sizes and business models. Of particular concern to us is the impact this could have on a FBO's ability to invest in start-up and early-generation companies or more established companies undergoing transformations. These companies often seek to establish business relationships with their investors, including FBO investors. A FBO investor, however, may be precluded from either making an investment at the size it and the investee would like or establishing business relationships because the business relationship test is evaluated at the outset and does not take into account anticipated growth in revenues as the investee grows or expands its business. To help alleviate this concern, we support the recommendation of BPI to provide a grace period of at least three years for applying the business relationship test to such companies, with the possibility of obtaining the Board's approval for additional one-year period extensions.

Asset-Backed Commercial Paper Conduits

Under Section 225.32(g) of the Proposal, the Board would presume that a company that consolidates a second company under U.S. generally accepted accounting principles ("GAAP") controls the second company for purposes of the BHC Act (the "Accounting Consolidation Presumption"). The Accounting Consolidation Presumption poses particular concerns for the MUFG Bank, Ltd., New York Branch ("MUBK NY") as the sponsor of two asset-backed commercial paper conduits ("Conduits" or "ABCP Customer Conduits"). The impact of the Accounting Consolidation Presumption on the Conduits would likely result in the termination or substantial reduction of this business for MUFG. This outcome would have serious adverse financial and competitive consequences for MUFG, its customers, and the ABCP markets, which rely on banks or branches of FBOs, like MUBK NY, for the safe and reliable provision of this working capital product.

Given the decades-long approach the Board has applied to the Conduits, which banks have relied upon to develop a significant business that provides stable, cost-effective, and transparent financing to important segments of the economy, the Board should not extend the Accounting Consolidation Presumption to the controlling influence framework of the BHC Act to these vehicles. There are compelling U.S. public policy reasons to protect the liquidity provided by these types of vehicles. If the Board does not withdraw the Accounting Consolidation Presumption from the Proposal, at a minimum, the Board should expressly exclude ABCP Customer Conduits from the application of the Accounting Consolidation Presumption. The Annex to this letter includes a detailed description of the Conduits, the role of MUBK NY in these markets, and the implications of the application of the Accounting Consolidation Presumption to the Conduits.

Joint Ventures

The Proposal provides in Section 225.32(a)(2) that "[f]or purposes of the presumptions in this section, any company that is a subsidiary of the first company and also a subsidiary of the second company is considered to be a subsidiary of the first company and not a subsidiary of the second company." The preamble to the Proposal indicates that this provision is meant to address relationships between companies that are subsidiaries of both the first and second companies (referred to as joint venture subsidiaries), on the one hand, and the second company, on the other hand, from being considered relationships between the second company and the first company when determining whether the first company controls the second company.[4] We understand that the intent is to allow companies to have joint ventures that, for purposes of the BHC Act, are controlled by both the first company and the second company without their

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4 Proposal at 21647.

respective control over the joint venture necessarily causing the first company to control the second company. The proposed rule text, however, addresses only the relationships between the first company and the joint venture subsidiary and not the relationships between the second company and the joint venture subsidiary when determining whether the first company controls the second company. As a result, as the proposed rule is drafted, the relationships between the second company and the joint venture would appear to be treated as relationships between the first company and the second company, because the joint venture is treated as a subsidiary of the first company and not of the second company. We believe a simpler approach to achieve the objective would be to permit the first company to exclude the relationships that both companies have with a joint venture subsidiary when determining whether the first company controls the second company.

Fund Seeding Period

In Japan, it is typical for institutional investors and pension funds to require a track record for newly created funds of at least three years, and often longer. Under the Proposal, the seeding period during which a company would not need to treat a fund it organizes and sponsors as controlled is limited to 12 months. The seeding period under the Volcker Rule for covered fund investment restrictions is a minimum of one year from the date of establishment of the fund with the possibility of an extension. For registered investment companies and foreign public funds, no application is necessary for an extension. We recommend that the permissible seeding period for an investment fund that a BHC or FBO organizes and sponsors be the same as the seeding period under the Volcker Rule.

Establishing a Balanced Control Framework

In addition to the specific proposals above, we urge the Board to incorporate in the final rule the following recommendations that would help restore a proper balance within a standardized framework between ensuring, on the one hand, that the Board appropriately captures "control" relationships and, on the other hand, without drawing in relationships that do not result in actual control or implicate the underlying purposes of the BHC Act control framework.

A. Investments Outside of the United States

When a FBO that is a qualifying foreign banking organization invests in a company that is located and predominately operates outside the United States, we believe that the Board should not apply the BHC Act control framework to that investment. Although there are many examples of how the imposition of the BHC Act control framework could upset non-U.S. activity even though the activity has no impact on the

United States,[5] we recognize that the final rule cannot and should not be written to take specific account of the laws, policies, and practices in all jurisdictions. We nonetheless believe that the Board should continue to recognize that, when making determinations about relationships between companies in other jurisdictions, consideration should be given to such differences. As noted, in the case of Japan, the Board specifically took account of the laws of Japan with respect to the scope of permissible relationships between FBOs and industrial or commercial companies and found that the FBOs were not controlled by the industrial, commercial, and financial companies with which the FBOs had interlocking stock ownership.[6]

An important element of our investments in companies that are located and predominately engaged in activity outside the United States are the investments we make, through funds for which one of our non-U.S. subsidiaries acts as general partner, in start-up and early generation portfolio companies in Japan. These investments are an important source of support for innovation and economic growth in Japan. For start-up and similar companies, venture capital investors often require contractual terms that are designed to protect the investor against the risk that the portfolio company would alter the terms of the investment or change its risk profile in a material way. Certain of these standard rights are included among the "limiting contractual rights" identified in the Proposal.

Because our investments relate to non-U.S. companies predominately engaged in activity outside the United States, we do not believe the investments need to be subject to the BHC Act control framework, as discussed above. We understand, however, that the same issue with respect to limiting contractual rights arises for U.S. BHCs. Accordingly, we support the specific recommendations in the letters of BPI and The Securities Industry and Financial Markets Association/The Financial Services Forum ("SIFMA/FSF") regarding changes to the scope of "limiting contractual rights."

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5 As just one example, in Japan there is a longstanding custom and practice across companies in all industries, including banking organizations, to introduce a member of its staff to its customers, at a customer's request, as a candidate to serve as a director, officer, or employee of the customer. When an appropriate candidate is identified, both the company and the customer expect that the company's employee will serve at the customer permanently. However, for a two-year period that is akin to a probationary period, the company and its customer share the costs of salaries and benefits of any referred staff. Although there is an expectation of permanent employment, the fact that the costs of the employee are shared for a two-year period, may result in the arrangement being treated as an interlock that could result in a control presumption under the Proposal if the employee serves as a senior management official of the customer.

6 See Japanese Bank Orders.

B. Presumptions of Non-Control

The presumptions in the Proposal relating to investors with a stake of 10-24.99 percent are automatic presumptions of control—that is, they identify what is impermissible rather than what is permissible. We recommend making the presumptions at all levels of voting stock ownership presumptions of non-control (akin to a safe harbor) to enhance certainty and transparency. In addition, this approach would avoid the circumstance in which an investor is automatically deemed to control a company simply because of a small or unexpected deviation from the presumption framework, such as, for example, a case where business relationships slightly exceed the applicable threshold in a given time period. At the same time, a framework that relies on non-control presumptions could afford the Board greater flexibility in administering the control framework, including greater latitude to take account of laws, policies, and practices in non-U.S. jurisdictions because making an accommodation would not require rebutting a control presumption. They would, of course, remain presumptions and not determinations of non-control.

C. Presence of a Larger Shareholder

The presence of a larger, unrelated shareholder has long been a factor in both formal and informal non-control determinations of the Board. Although there are many ways in which the Board could recognize the countervailing force of a larger shareholder, at a minimum there should be a presumption of non-control if there is a shareholder unrelated to the investor that owns 50 percent or more of the same class of voting stock as the investor. This is a clear and reasonable standard that would be easy to apply. A shareholder with a majority in almost any circumstance should be able to preclude a controlling influence of an investor with a less than 25 percent voting stake.

D. Simplifying Equity Ownership Calculation

Under the Proposal, when a first company has an investment in the parent company of the second company (as well as in the second company itself), the first company must include the total equity it holds of the parent company when calculating total equity for purposes of determining whether it is presumed to control the second company. Because the first company may have only a small equity stake in the parent and the parent and second company may not be subject to the BHC Act, we recommend that a first company only include in the calculation an equity stake in a parent that owns 25 percent or more of the second company. Obtaining sufficient information to conclude whether the parent's relationship with the second company would trigger a control presumption may in some cases be difficult to obtain, at least at the level of specificity

necessary to evaluate the relationship under the Proposal. Applying this objective test would simplify compliance efforts significantly without undermining its purpose.

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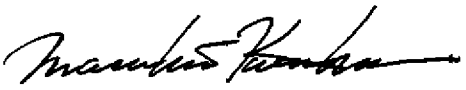
We appreciate the opportunity to provide comments and would be happy to discuss them further or provide additional information. Should you have any questions, please contact Tomohiro Ishikawa, Managing Director, Head of Global Regulatory Affairs Department, Corporate Planning Division, at +81-3-3240-7885, Roger Blissett, Head of Government and Regulatory Affairs for the Americas, at (212) 782-4704, or the undersigned.

Sincerely,



Masahiro Kuwahara
Managing Corporate Executive,
Group Chief Risk Officer

Annex

The Accounting Consolidation Requirement Should Not Apply to ABCP Customer Conduits

The ABCP Customer Conduits were organized in the 1990's and, like other similar vehicles sponsored by the major U.S., Japanese, Canadian, and European banks, are well-established vehicles for financing financial assets in the real economy. The ABCP Customer Conduit market is a significant contributor to the financing of a wide variety of consumer and commercial asset types that allow for increased lending to important segments of the economy, including industrial and service companies and governmental entities. MUBK NY's ability to originate new business in challenging economic environments has been instrumental in the rise of MUBK NY in the conduit market league tables. Commercial paper of our Conduits continues to be issued in significant volumes and at attractive financing rates.

The exclusive business of the ABCP Customer Conduits is to issue commercial paper backed by pools of receivables and loans originated by unaffiliated bank customers of MUBK NY. The bulk of the Conduits' assets are trade receivables wherein customers finance their working capital through short term conduit financing and where the asset liability match is optimal. The Conduits also engage in automobile loan and lease financing primarily for retail consumer assets originated by MUBK NY client auto companies. Unlike Structured Investment Vehicles ("SIVs") and certain other types of conduits, the ABCP Customer Conduits have no exposure to mortgage products, structured products such as CLOs or any types of securities.[1] The business of the Conduits is an integral part of MUBK NY's product offerings to meet the financing needs of its clients.

MUBK NY performs customary activities as a bank sponsor of the Conduits, including marketing the securitization product to its clients, performing due diligence with respect to the asset pools, and arranging the financing transactions with the clients who originated those assets.[2] On the Conduits' liability side, MUBK NY administers the Conduits' asset-liability position and directs placement of the commercial paper in the capital market with end investors through commercial paper dealers.

MUBK NY also extends two back-stop facilities to the Conduits that provide both credit and liquidity support. Each facility is extended on an arm's length basis and is non-exclusive. The Conduits are viewed as creditworthy by MUBK NY's risk management group independently of any connection with MUBK NY.

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1 ABCP Customer Conduits that finance bank client assets are fundamentally different from SIVs and other conduits that financed purchases of securities prior to the financial crisis.

2 Functions performed by MUBK NY include obtaining the mandate, structuring the deal, gathering information for providing due diligence on the assets, working with legal teams to document the deal, modeling cash flows, obtaining internal credit approvals, and a myriad of other tasks.

As a sponsoring bank, neither MUBK NY nor any of its affiliates, directly or indirectly:

- Owns, controls, or has the power to vote any class of voting securities of the Conduits (or of its unaffiliated equity owners);
- Controls in any manner the election of directors of the Conduits; and
- Exercises a controlling influence over the management policies of the Conduits.

Each of the Conduits has its own board of directors selected by its unaffiliated equity owners and no individual affiliated with MUBK NY sits on these boards. Each board is responsible for the oversight of the Conduits.

The Conduits are consolidated with MUBK NY under GAAP because they are within the scope of variable interest entity ("VIE") consolidation rules.[3] However, the Conduits are not consolidated under Japanese GAAP. The introduction of a GAAP approach in the controlling influence framework of the BHC Act results in the Board ceding to the Financial Accounting Standards Board ("FASB"), a non-governmental organization, the ability to determine control standards in a context where the underlying objectives of FASB rules materially differ from those of the BHC Act.

The substantially harmful impact of a control determination with respect to the Conduits results from the application of the Board's Regulation YY to FBOs. Under Regulation YY, MUFG is required to hold its "ownership interests" in all U.S. subsidiaries under its U.S. Intermediate Holding Company ("IHC"). Regulation YY does not define "ownership interest." If the Board were to retain a presumption of control under the Accounting Consolidation Presumption, the Board should confirm that ownership interests under Regulation YY include only equity interests in the Conduits and not the liquidity facilities that result in GAAP consolidation of the Conduits with MUBK NY. This approach would be consistent with the non-control position taken by the Board in 2015 in the context of implementation of Regulation YY, which allowed FBOs to maintain their respective conduits independent of their IHCs.

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[3] ABCP Customer Conduits are treated as VIEs because the small amount of equity capital typically provided to the Conduits means that the total investment at risk is generally insufficient to permit these vehicles to fund their activities without additional credit and liquidity support that generally act to insulate the equity owners from significant losses. Sponsor banks are usually the entities that are required to consolidate the Conduits because of the nature of the credit and liquidity facilities, as well as the nature of the services they provide. These liquidity facilities are treated as "variable interests" by MUBK NY in the Conduits.

Transferring these facilities to our IHC or to MUFG Union Bank, N.A. ("MUB"), the regional bank, would likely result in the termination of our Conduit business. The ABCP conduit investor base places conduits on their approved list based primarily on the credit rating of the liquidity provider. The liquidity provider must be a major global bank recognized as an experienced conduit sponsor and be rated A-1/P-1 by S&P and Moody's, respectively, and neither our IHC nor MUB have the ratings or the independent funding ability to provide the requisite liquidity. In the unlikely event that investors were to accept MUB or the IHC as providers of backstop facilities, both entities would need to rely on MUBK NY as the ultimate liquidity provider given the substantial size of the Conduits. As a regional bank, MUB's business model and risk profile would be substantially altered if it took on the function of liquidity provider. In addition, if the Conduits were consolidated with the IHC but financed by MUB, the liquidity facilities would become unfeasible as covered transactions under the Board's Regulation W.

The activities conducted by MUBK NY in connection with the ABCP Customer Conduits are adequately and substantially regulated and supervised by the Board, the OCC, and the Japanese Financial Services Agency. MUFG Bank, Ltd. is generally required to maintain regulatory capital against the full amount of MUBK NY's commitments to the Conduits under the risk-based capital rules (whether funded or unfunded), and is required to maintain highly liquid assets on a dollar-for-dollar basis against the amount of commercial paper notes that mature within 30 days under the home-country liquidity coverage ratio rule. In addition, MUBK NY includes the liquidity facilities in the calculation of its high-quality liquid assets buffer requirement under Regulation YY.

For the reasons discussed above, if the Board does not withdraw this presumption from the Proposal, at a minimum the Board should expressly exclude ABCP Customer Conduits from the application of the Accounting Consolidation Presumption.